No. 21,795

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

ESTATE OF EUGENE L. FREELAND, Deceased, by SECURITY FIRST NATIONAL BANK, a national banking association, Executor, and VERA GOOD FREELAND, by L. N. TURRENTINE, Conservator,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR REHEARING.

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Petitioners now petition this Court for rehearing, upon the grounds stated below. Petitioners submit that at least this case should, under 28 U.S.C. §2106, be remanded to the Tax Court for further proceedings so that that Court may reexamine the record, and that Court and the parties take any other proper procedures, from the standpoint of the grounds for this petition stated below.

Petitioners also suggest, under Rule 23(5) of this Court, that this case should be reheard en banc, chiefly because of the uncertainties, pointed out below, expressed this Court's opinion, and the doubt of respondent himself, pointed out in paragraph 6 below, that this Court's opinion supports its judgment.

Grounds of Petition.

The grounds of this petition are solely errors of law on the face of this Court's opinion, and conflicts between its opinion and its judgment, as follows:

1. This Court, at page 17[1], quotes, and appears heavily to rely upon, several factual inferences of the Tax Court. Such inferences, if not "mere suspicion," but factual conclusions based on "informed experience with human affairs," would come within the "clearly erroneous" rule. *Commissioner v. Duberstein,* 363 U.S. 278, 292, 80 S. Ct. 1190, 1200. The inferences here, however, are framed in the very language of suspicion. Nor do they indicate a basis of informed experience.

For example, as shown at p. 5, the 4500 acres, a mere seven square miles, "contained a lake, some canyons, and a mountain rising about 1100 feet above the surrounding terrain." Also, as to the mountain, the cost of off-site improvements, as shown at p. 13, was found to be prohibitive even at the foothills. Simple arithmetic would show that even with an average slope as high as 25%,[2] the mountain alone, with a floor radius then of 4400 feet, would rule out as unusable one-third of the 4500 acres. Yet the Tax Court used SBIC's average cost per acre based on the entire 4500 acres in order to treat its selling price to LMDC as a scheme for despoiling the federal revenue.

We give the above only as one example of the character of the inferences made. Most of the others cited at p. 17 are of like character. We submit that those inferences, just as their very wording shows, do not rise above the level of mere suspicion.

2. This Court states, at p. 18, that, as to SBIC's original purpose, the Tax Court "might possibly have

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[1]The page references herein, if not otherwise identified, are to this Court's slip opinion.

[2]The maximum grade provided in San Diego is 15%. Council Resolution No. 173217.

properly found in petitioners' favor"; and that, as to petitioners' contentions of change of purpose, they "are admittedly not without support," and there would "perhaps have been considerable basis for a finding" in accordance with them. But, this Court says, at p. 19, the burden of proof was on petitioners.

What is required of petitioners because of their burden of proof is the preponderance of the evidence, evidence therefore showing that the facts asserted by them are more probably true than false. *Burch v. Reading Co.* (C.A.3), 240 F. 2d 574, 579, cert. denied 353 U.S. 965. The Supreme Court has stated that requirement as the evidence which "would reasonably support a verdict for a plaintiff in an ordinary action for the recovery of money." *Burnett v. Niagara Falls Brewing Co.*, 282 U.S. 648, 654, 51 S. Ct. 262, 265; 2 Casey's Federal Tax Practice §8.7 at fn. 45, 9 Mertens §50.62 at fn. 23. We submit that what this Court has in fact said here, in effect, is that petitioners have carried their burden of proof.

The burden of proof rule, moreover, may not be applied to defeat justice. *Helvering v. Taylor,* 293 U.S. 407, 55 S. Ct. 287, 9 Mertens §50.62 at fn. 22, §50.65 at fn. 60. Clearly, this Court's own statements, quoted above, show that the evidence was adequate to support petitioners, so that a decision against them would be inconsistent with justice. This is true here all the more because the tax asserted would, as shown in our opening brief, at pp. 10-11, consume the entire estate. It is also emphasized by the Tax Court's recent contrary decision in *Ronhovde v. Commissioner,* 26 T.C.M. 1251, cited and summarized in our reply brief at p. 7.

3. This Court states, at p. 18, that the "clear purpose of denying capital gain treatment to profit attributable to the sale of inventory is to prevent the owners of businesses yielding ordinary income from in effect reducing their tax liablity on such income merely

by selling their businesses *in toto.*" In the first place, there is no evidence or experience supporting the idea that a person would be likely to dispose of a business yielding income just to reduce his tax liability. In the second place, the clear purpose of the statutory provision, as found by the Supreme Court, was to deny capital gain treatment to the "profits and losses arising from the everyday operation of a business." *Corn Products Refining Co. v. Commissioner,* 350 U.S. 46, 52, 75 S. Ct. 20, 24. The sale of a business *in toto* could hardly be the same as the everyday operation of the business.

In the third place, this Court, in its statement quoted above, by using the term "inventory" clearly begs the question. So this Court does again when it next says that denial of capital gain treatment to inventory "would in many instances be frustrated if an intention to 'liquidate' such a business sufficed to establish the sort of 'change of purpose' which petitioners contend occurred here." The land involved here, if classified as inventory during the relevant period, would be so classified only if it was then held primarily for sale to customers in the ordinary course of the taxpayer's trade or business. This Court, at pp. 2-3, makes that point clear. Therefore, to speak of the property involved here as inventory begs the very question at issue here, whether during the relevant period it was inventory.

In the fourth place, and more important still, there is no finding here of sale of a business, or *in toto.* The sale in each case was only of an interest in the partnership, SBIC. Thus after the sale by Berger the land was still held in partnership.[3] But there was a very important change. Berger, the promoter, Berger, the partner upon whose statements and activities the Tax

[3]This would also be true if the land was regarded as thereafter held by a constructive successor partnership resulting from the sale. Treasury Regulations, Sec. 1.708-1(b)(1)(iv).

Court almost wholly relied for its conclusion as to original purpose, he was out, and Freeland, the only remaining general partner, refused to join Berger's vendee in development of the property. (Pp. 5, 9, 14.) The situation was the same in effect as if Berger had died. Calif. Corp. Code §15520. Whether liquidation followed or not, the purpose of holding the land after Berger's sale could not be tied to the purpose before. *Estate of Ferber,* 22 T.C. 261, 264, formally acquiesced in by respondent, 1954-2 C.B. 4. See also *Greenspun v. Commissioner* (C.A. 8, 1956), 229 F. 2d 947, 953, 46 A.L.R. 2d 615, 706 §24 at fn. 19.

4. At pp. 18-19, this Court finds it "quite conceivable" that, during the period after Tavares' entry into SBIC, SBIC's purpose regarding the land "was to some degree not clearly defined." This Court does not say there that the *evidence* was unclear. What this Court plainly says there is that what the evidence did establish was that SBIC's purpose, which it would find as a "legal construct" in SBIC's composite mind, was not, in that mind itself, clearly defined.

With this we need not disagree. The purpose regarding the land required to support respondent's determination was a purpose, of SBIC, during the period above referred to, to hold the land "primarily for sale to customers in the ordinary course of [its, SBIC's,] trade or business." I.R.C. 1954, Sec. 1221(1). The burden of petitioners was therefore to prove that sale to customers in the ordinary course of SBIC's trade or business was not SBIC's *primary* purpose regarding the land during that period. But if SBIC's purpose regarding the land was not clearly defined *in SBIC's own mind,* that purpose could be substantial but not primary. See, in Professor Kenneth Burke's monumental work entitled "A Grammar of Motives," the analysis, pp. 51-53, under the subtitle "The

Rhetoric of Substance."[4] Petitioners' burden was therefore fully carried if their proof was that SBIC's purpose "was to some degree not clearly defined."

5. The "clearly erroneous" rule upon which this Court relies, at p. 19, does not apply, it is clear, to a finding induced by an error of law. *Hoover Co. v. Mitchell Manufacturing Co.* (C.A. 7, 1959), 269 F. 2d 795, 808; *Municipal Bond Corporation v. Commissioner* (C.A. 8, 1967), 382 F. 2d 184, 188. We submit, therefore, upon the basis of the errors of law shown above, that the "clearly erroneous" rule has no application here.

6. Respondent himself apparently is concerned that this Court's opinion does not support its judgment of affirmance. On March 28, 1968, after two extensions of time, the government filed in the United States Court of Claims, in docket Nos. 70-65 and 73-65 there, being suits for refund by other partners of SBIC involving the same issue as here, a brief citing several times, and discussing, the case here as decided by the court below, and noting its pendency here on appeal, but making no reference to the opinion or decision therein of this Court, although obviously available to the government long before said brief was filed.

Respectfully submitted,

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[4]Professor Burke was visiting lecturer at Harvard during its 1967-1968 year.